March 7, 2005 Tax reform is back in the news, brought to the political forefront by a recent meeting of the president’s advisory panel on tax reform. Once again, politicians and former politicians are lamenting the complexity of our tax laws, as though their own spending measures have nothing to do with it. But we’ve heard this song before. In fact, we’ve been promised a simpler, fairer, and better income tax system many times, most recently in 1997 and 1986 when Congress made relatively significant changes to the tax code. Yet the federal tax system remains an embarrassment, both in terms of the tax burden itself and the outrageous compliance costs engendered by its complexity. One tax reform idea tacitly endorsed by Federal Reserve chairman Alan Greenspan calls for a national retail consumption tax to replace the existing income tax. Absent the outright repeal of the 16th Amendment, however, we cannot be sure that an income tax would not reappear at some point. One can easily imagine popular support for retaining the income tax on the “very rich,” which of course is how the 16th amendment originally was sold to a gullible public in the 1910s. The president has thrown cold water on the consumption tax proposal, however, by announcing he opposes any reform that eliminates mortgage and charitable deductions. This leaves us with variations on the flat tax concept, which was savaged by the political left when advocated by the likes of House Majority Leader Dick Armey and Steve Forbes in the 1990s. Lew Rockwell of the Ludwig von Mises Institute offers a very simple test for any tax reform proposal: Does it reduce or eliminate an existing tax? If not, then it amounts to nothing more than a political shell game that pits taxpayers against each other in a lobbying scramble to make sure the other guy pays. True tax reform is as simple as cutting or eliminating taxes. No studies, panels, committees, or hearings are needed. When reform proposals seem complicated, they almost certainly don’t cut taxes. The reform debate is strictly about politics and not serious economics. Both sides use demagoguery but don’t propose truly significant tax reductions. Both sides use the outrageous expression “cost to government” when talking about the impact of tax legislation on revenues. This implies that government owns everything, and that any tax rate less than 100% costs government some of its rightful bounty. Government spending is the problem! When the federal government takes $2.5 trillion dollars out of the legitimate private economy in a single year, whether through taxes or borrowing, spending clearly is out of control. Deficit spending creates a de facto tax hike, because deficits can be repaid only by future tax increases. By this measure Congress and the president have raised taxes dramatically over the past few years, despite the tax-cutting rhetoric. The real issue is total spending by government, not tax reform.

Who wants a 40% flat tax? Who wants a national sales tax if it adds 35% to the retail price of everything we buy? In other words, why change the tax structure if spending stays the same? Once we accept that Congress needs $2.5 trillion from us-- and more each year-- the only question left is from whom it will be collected. Until the federal government is held to its proper constitutionally limited functions, tax reform will remain a mirage.